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SIPDIS
SENSITIVE

STATE FOR EEB/IFD/OMA
STATE FOR EEB/EPPD
DEPARTMENT PASS TO USTR AGAMA
TREASURY FOR PETERS, IERONIMO, HALL
USDA/FAS/OTP FOR MCKENZIE
SECSTATE PASS TO USAID/AFR FOR ATWOOD
DOC FOR 3317/ITA/OA/KBURRESS AND 3130/USFC/OIO/ANESA/DHARRIS

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TAGS: EFIN ECON EINV EPET ENRG EPET PGOV NI
SUBJECT: GLOBAL FINANCIAL CRISIS IMPACTING NIGERIA

REF: A. STATE 134459
¶B. ABUJA 2437
¶C. LAGOS 520
¶D. ABUJA 2386
¶E. ABUJA 2387
¶F. ABUJA 2365
¶G. ABUJA 2180
¶H. LAGOS 426

¶1. (SBU) Summary. This cable responds to ref A tasking. Despite the Nigerian government's (GON) public statements, the global financial crisis (GFC) has impacted Nigeria in its most vulnerable area - revenue from crude oil sales. Crude oil accounts for over 80% of government revenue and over 90% of export earnings for Nigeria and the drop in demand for oil and the resulting fall in oil prices is hurting Nigeria. According to the GON, the slowdown in economic growth, the rise of inflation and naira depreciation are just cyclical trends that would have taken place without the GFC. GON officials have expressed confidence in public that this slowdown will not last a long time. The key effects on the Nigerian economy are: less income from crude oil sales have led to less revenue for the FY 2009 budget; a reduction in the flow of funds to Nigeria from foreign investors; the drop in the oil price has decreased consumer spending; and the Nigerian stock market has lost nearly half its value since February 2008, which dampens lending. As a result of the fiscal impact, in FY 2009 the GON will operate with a projected budget deficit of 1.1 trillion naira ($7.4 billion), which constrains fiscal spending. Considering the large sums needed to improve electricity supply and infrastructure, difficult decisions will have to be made on spending priorities. Decreases in government spending will affect the implementation of the Millennium Development Goals (MDG), which was already falling short of the country targets. Millennium Development Budget (MDB) may see a reduction in funds from the GON and donor community. The GON needs to demonstrate political will to ensure proper allocation of resources, not only for MDG but the whole economy. In response to this widening impact, on January 13, 2009 the GON created a Presidential Steering Committee chaired by President Yar'Adua to assess among other things, the impact of the GFC on Nigeria and appropriate responses (septel). End Summary.

Don't Believe the Hype

¶2. (SBU) The global financial crisis including the fall in oil prices have a major impact on the amount of resources that Nigeria has available for investment in infrastructure and building the capacity of institutions at the federal, state and local government

levels. Even with decreasing resources, GON officials are cautious when discussing the GFC and reiterate comments that the GFC has not had and will not have a major impact on the Nigerian economy. In their view the economy is experiencing "light turbulence." In December 2008 Merrill Lynch reported in a review of the Nigerian economy in 2008 that Nigeria has fared better than most emerging markets whose economies are more globally integrated. This report was widely cited in local newspapers and in government broadcasts. Based on Nigeria's second quarter 2008 data, the report noted that Nigeria's Gross Domestic Product (GDP) growth of 6.4% was higher than the 4.5% average growth for 26 emerging market economies (EME) including China, India and Russia (reftel C).

Reduction in Oil Production

¶3. (SBU) Falling oil prices coupled with tighter credit markets will likely lead to a further erosion of oil production in Nigeria and continued deterioration of existing petroleum infrastructure. At least two large international oil companies have reduced or flat lined their operating budgets for 2009 and we expect all oil companies are taking a close look at the operating profiles in Nigeria. Companies are likely to defer maintenance projects and forgo new exploration and production ventures. Wells that are shut in due to sabotage may not be reopened as quickly, if ever. While last year, companies such as Shell and Chevron extended credit to the GON to finance its share of oil production costs, similar financing in 2009 may be tougher to arrange. In addition, Nigeria had planned to restructure its oil production joint ventures, forcing them to seek outside financing instead of government and oil company financing. That plan will be even harder to implement in the current credit market. The impact of all these factors could

mean that oil production remains far below its potential for several years, even if oil prices recover. On the natural gas side, we can expect new natural gas projects, such as the Brass and OK Liquefied Natural Gas Projects, to be delayed or even cancelled. Similarly, movement towards eliminating natural gas flaring in Nigeria is likely to slow.

Naira Sliding

¶4. (SBU) The naira had recorded relative stability since 2005, but has now greatly depreciated against the dollar; between November 2008 and January 13, 2009, it has moved from 117 naira per dollar to 153 naira per dollar. Due to the GFC, foreign banks are calling in credit lines that were earlier approved for Nigerian banks (reftel E). As reported to the press by the Director General of the West African Institute for Economic and Financial Management, Nigeria has lost over $4 billion to "panic divestments" by foreign investors. Falling foreign exchange holdings have increased oversight by the Central Bank of Nigeria (CBN) of Nigerian banks and the CBN has issued new guidelines that reduce bank foreign exchange net holdings from 20% to 10% and require further documentation during forex purchases to hamper banks hoarding dollars for speculative gains. The CBN expects that these actions will stabilize the foreign exchange market and renew confidence in the naira (reftel B).

Budget Shortfall

¶5. (SBU) The crisis has led to substantial reduction of the FY 2009 budget given the expected fall in revenue earnings from oil. In December 2008, President Yar'Adua presented the 2.87 trillion naira ($24.53 billion) budget for FY 2009. The proposed budget sets crude oil production at 2.292 million barrels per day (mbpd) and a benchmark price of $45 per barrel (reftel F). A major drop in revenues may lead to a significant cutback in the Millennium Development Goals (MDG) grants to states, which are increasingly important incentives to state governments. (Comment: The Mission has not seen any sign of things amiss in the MDG program plan, though we are cultivating contacts to see if that is the case. End Comment)

GFC Impact in Financial Sector

¶6. (SBU) Most bankers and other financial sector officials agree that the financial crisis is having the following effects on the Nigerian economy:
-- Reduction in the flow of funds to Nigeria from external funding sources (foreign remittances, foreign direct investment, credit lines from multilateral institutions/banks, non-oil exports, donor funds);
-- Major drop in the price of oil causing decrease in consumer spending;
-- Nigerian stock market has lost value which affects lending based on securities as collateral.

¶7. (SBU) Some banks indicate that their institutions are not facing serious ramifications yet due to strong deposit bases while other indicate that their cost of funds , as well as lending rates, had increased which will result in less lending in 2009. (Comment: It is not possible to ascertain the health of the Nigerian banking system as most banks engage in under the table activities to shore up their balance sheets. Banks tend to exaggerate their levels of growth and performance and such statements cannot be taken at face value. End comment.) Banks are offering fewer mortgages at higher interest rates, while some refuse to offer any altogether. Deposit rates have increased, according to one estimate from 11% to 16% for 10 million naira ($66,666) deposits. (Comment: Up to this point, high lending rates and low deposit rates have been an accepted fact of doing business in Nigeria. End Comment.) According to industry sources, in August 2008 banks were getting comfortable with the idea of medium term financing, but now are retreating given the drying up of liquidity in the international and domestic markets.

¶8. (SBU) Drop in the stock exchange is seen by the Nigerian financial market regulators as a "market correction" and not a symptom of larger problems. Since February 2008, market capitalization declined from 12 trillion naira ($102 billion) to nine trillion naira ($76 billion) by the end of October 2008. (reftel G). Policies are presently being developed to assist

companies whose shares have suffered a free fall to cope and protect stock holders from bankruptcy.

¶9. (SBU) International organizations are more realistic in their reports when it comes to the GFC impact. The International Monetary Fund (IMF) reported in November 2008 that Nigeria's economy is slowing down because falling oil prices will push GON revenues downward. IMF also forecasts rising inflation (reftel D).

Millennium Development Goals

¶10. (SBU) Given the nature of the development partner relationships with the GON and the dynamics of the scale of donor funding with the GON budget, the U.S. Mission in Nigeria is unaware of any moves to accelerate MDB disbursements on projects given the crisis. Depending on the ultimate depth and length of the recession in different countries, there may be sector effects that will exacerbate already existing under-investment, particularly in health and education.

¶11. (SBU) While not having seen data from the GON (federal or state) about direct reduction in or reprioritizations of funding for HIV or TB related initiatives, one could presume the sector as a whole may be vulnerable from three aspects: reduction in funds from GON, decrease of funds from donor community, and increase in risky behavior due to downturn in economy.

¶12. (SBU) Reduction in funds and resources such as commodity procurements and pharmaceuticals available at the Federal or State levels for the HIV and TB response might result in increased demand for donor supports for maintenance of current programs.

¶13. (SBU) Decreased availability of funding from other donors may specifically come into play with regard to Global Fund support (i.e., further restrictions on the funds available for Round 9

proposals which are key for both the HIV and TB response in Nigeria) due to drops in multilateral contributions to the fund across the board.

¶14. (SBU) Generalized economic downturn may increase individual vulnerabilities, leading to increasing susceptibility to HIV infection through risky behaviors such as commercial/survival sex work, increased migration in search of economic opportunity leading to disruptions in protective familial structures and reduced ability to seek/maintain regular medical assistance for HIV+ people in care/treatment.

¶15. (SBU) Prior to the GFC, the GON responded to the emergent Global Food Security crisis and expanded its focus on creating jobs and economic wealth in the agricultural sector. An overall slow down in revenue is likely to limit the capacity of the GON to provide sufficient resources for seeds, fertilizer and to expand their mechanization programs. The GON, donors and International Financial Institutions, which are in the process of developing a 3 three year Country Partnership Strategy that includes a focus on expanding non-oil sector growth, will take on a heightened importance. The USG response of a $25 million Global Food Security Response program in Nigeria will not be sufficient to offset the reduction in revenues and the GON is likely to ask the USG to continue its support at comparable levels over the next few years.

Comment

¶16. (SBU) The GFC and the fall in oil prices may impact on the amount of resources that many African governments, including Nigeria, will have for investing in infrastructure and building the capacity of their institutions, especially governance institutions at the federal, state and local government levels. There are fears that the gains already recorded in fiscal policy reforms may be lost due to dwindling resources that may be available to the GON. Nigeria's economic and political reforms are at a point where the government needs to demonstrate political will as well as ensure the allocation of appropriate resources for effective implementation of its reforms.

¶17. (U) This message was coordinated with ConGen Lagos.

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